

Photocopiers are specifically excluded from the graphic arts machinery and equipment exemption and their sales are subject to Retailers' Occupation Tax and Use Tax. See 86 Ill. Adm. Code 130.325(c)(4)(E). (This is a GIL).

May 13, 1999

Dear Xxxxx:

This letter is in response to your letter dated May 7, 1999. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

COMPANY and subsidiaries hereinafter referred to as Lessee is investigating the Sales and Use Tax treatment of a lease transaction involving tangible personal property that will have a taxable situs in your state.

We hereby request a ruling to clarify the application to your state sales and use tax law with respect to the transaction and equipment described below.

The equipment in question, Xerox 5750 Color Copier machine was originally purchased by the Lessor for subsequent lease or rental. The Lessee may enter into a 'True Lease' agreement with the Lessor, length of term still to be determined. Title to the property will remain with the Lessor, the owner of the property for Federal Income Tax purposes.

The Xerox 5750 Color Copier machine will be installed on site in our retail store locations. The installation will be behind our camera photo counter and are not accessible to our customers. COMPANY employees will accept the customers' orders and process the orders of making the copies. Once orders are complete, sales will be registered at our camera photo counter cash registers.

The machine has the following capabilities:

- 1) Color and Black & White heavy weight paper for posters, Reprint Covers and etc.
- 2) Reverse Image
- 3) Change the color Black to any color, color conversions (i.e. Orange to Green)

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- 4) Delete Information
- 5) Sizes available are from Postcard Size to 11 X 17 inches
- 6) Photo Retouching

The Lessee's primary business is operation of retail drug stores, but we believe that a Sales and Use Tax exemption may qualify based on the type and/or process use of the equipment under Manufacturing, Industrial Processing or Printing statutes or other provisions existing in your state.

We respectfully request your review of the facts presented and situations within this letter. We also request a ruling as to the taxability of supplies used in the producing copies such as toner, paper and etc., and the taxability of the final product sold to our customers. Also we would appreciate you furnish us authority for your response (statue, regulations, rulings, opinions, and etc.). We certainly appreciate your assistance in this matter. If you have any questions or need any additional information, please call me at ####.

Please be advised that the Retailers' Occupation Tax does not apply to the sale of machinery and equipment, including repair and replacement parts thereof, to be used primarily in graphic arts production. See, 86 Ill. Adm. Code 130.325, enclosed. Photocopiers are specifically excluded from the graphic arts machinery and equipment exemption and their sales are subject to Retailers' Occupation Tax and Use Tax even though this equipment may be essential to production. See 86 Ill. Adm. Code 130.325(c)(4)(E), enclosed. Therefore, sales of color copiers are subject to the Retailers' Occupation Tax and Use Tax.

Generally, photocopiers do not qualify for the manufacturing machinery and equipment exemption. See 86, Ill. Adm. Code 130.330, enclosed. Please note that in order to qualify for the manufacturing machinery and equipment exemption, the machinery or equipment must be used primarily in a manufacturing process that is commonly regarded as manufacturing.

In Illinois, lessors of tangible personal property under a true lease, except for automobiles leased for terms of one year or less, are considered to be the end users of the property to be leased. See the enclosed copies of 86 Ill. Adm. Code 130.220 and 130.2010. As the end users of tangible personal property located in Illinois, lessors incur Use Tax on the lessors' cost price of the property. Since lessors are considered the end users of the property and have paid the Use Tax, no Retailers' Occupation Tax is imposed upon the rental receipts and the lessees incur no Use Tax liability for the rental charges. In Illinois, a true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease.

The alternative to a true lease is a conditional sale. In Illinois, a conditional sale is usually characterized by a nominal purchase option at the close of the lease term. This type of transaction is considered a conditional sale at the outset of the transaction making all receipts subject to Retailers' Occupation Tax. See Section 130.2010. In this situation, lessors/retailers may give Certificates of Resale to their suppliers for tangible personal property transferred subject to a conditional sales agreement. The lessors/retailers owe Retailers' Occupation Tax on any installment payments when they are received by the lessors/retailers. The lessees/purchasers owe corresponding Use Tax on the amount of the installment payments that are collected by the lessors/retailers.

As stated above, lessees do not incur any tax liability in a true lease situation. However, it is typical of true leases to contain contractual provisions stating that the lessees will *reimburse* the lessors for their tax costs. This is not a matter of Illinois tax law but of private agreement between lessors and lessees. If the lessees agreed to such provisions, they are bound to satisfy that duty because of a contractual agreement, not because of Illinois tax law.

Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred as an incident to sales of service. See the enclosed copy of 86 Ill. Adm. Code 140.101. The purchase of tangible personal property that is transferred to the service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon which tax base the servicemen choose to calculate their tax liability. The servicemen may calculate their tax base in one of four ways: (1) separately stated selling price of tangible personal property transferred incident to service; (2) 50% of the servicemen's entire bill; (3) Service Occupation Tax on the servicemen's cost price if the servicemen are registered *de minimis* servicemen; or (4) Use Tax on the servicemen's cost price if the servicemen are *de minimis* and are not otherwise required to be registered under the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If the servicemen do not wish to separately state the selling price of the tangible personal property transferred, the servicemen must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred.

The third way servicemen may account for tax liability only applies to *de minimis* servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Serviceman may qualify as *de minimis* if the servicemen determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the servicemen's annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). This class of

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registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to the sale of service. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if the servicemen determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the servicemen's annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. The servicemen are not authorized to collect "tax" from their service customer nor are the servicemen liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis.

Servicemen calculating their tax using the first three methods mentioned above may give resale certificates for the paper and toner that they purchase for color copiers that generate copies for sale. De minimis servicemen using the fourth method may not give resale certificates for such supplies.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Gina Roccaforte
Associate Counsel

GR:msk

Enc.